

CITY OF PUYALLUP
Pierce County, Washington
January 1, 1993 Through December 31, 1993

Schedule Of Findings

1. Public Funds Were Misappropriated And Accounting Records Were Falsified And Destroyed

Our audit of the financial records of the recreation center at the City of Puyallup revealed that at least \$2,167.75 in public funds were misappropriated by one or more employees during the period April 1, 1993, through May 31, 1994. Accounting records were falsified in an attempt to conceal these losses. There were no federal funds involved in this case.

During normal review and monitoring activities by the City of Puyallup, the finance department determined that cash receipts were not being properly accounted for at the recreation center. As a result, the Office of State Auditor was notified of irregularities in the recreation center's bank deposits in May 1994. We immediately commenced a special audit of cash receipts at the recreation center and confirmed that a misappropriation of public funds had occurred.

The schedule below summarizes these losses by source of the misappropriated funds:

<u>Description of Loss</u>	<u>Amount</u>
Short Deposits	\$1,126.60
Fictitious Void Transactions	335.25
Unrecorded Cash Receipt Transactions:	
Check For Cash Substitution Scheme:	
Checks From Vendors	85.90
Checks From Customers	620.00
Missing Funds After Computer Cash Register Merge Failure	<u>Unknown</u>
Total Losses	<u><u>\$2,167.75</u></u>

These funds were misappropriated as described below.

- a. Short Deposits The amount of currency and checks included in the recreation center's bank deposits did not always equal the amount recorded on the bank deposit slip or the fund accountability recorded on the computer cash register system reports. Cash register tapes of the checks accompanying these bank deposits were falsified to indicate a total amount which was higher than actually included in the deposit. When these conditions were noted by the bank during the

proofing process, a debit memorandum was prepared for the deposit shortage and forwarded to the city finance department. All falsified bank deposit records were prepared by only one person, the office specialist. These short deposits were made on eight deposits in 1994 and on one deposit in 1993. The amount of loss from this method was \$1,126.60.

- b. Fictitious Void Transactions After cashiers recorded valid transactions on the computer cash register system, these transactions were subsequently voided to eliminate accountability for the funds. There were no supporting documents retained on file at the recreation center for these void transactions. In addition, management did not require these high risk transactions to be approved by a supervisor. Since these transactions were valid, all customers actually received the service provided by the recreation center. In one case, a customer whose valid transaction had been fraudulently voided actually received a refund from the city because a sufficient number of participants had not registered for the class involved. This refund resulted in an additional loss of funds at the recreation center because no revenue had been officially recorded on the computer cash register system from this source. Customer checks from these valid transactions were also included in the recreation center's bank deposit using a check for cash substitution scheme as further explained below. These fictitious void transactions were made on both the morning and afternoon shifts for seven of the 1994 business days reviewed during this audit. The amount of loss from this method was \$335.25.

- c. Unrecorded Cash Receipt Transactions Employees did not always record accountability for all revenue received by entering these transactions on the computer cash register system at the recreation center. Any employee could pick up the mail and process these high risk revenue transactions. In addition, no one independent of the cashier function opened the mail and made a list of these revenue transactions for control purposes.

(1) Check For Cash Substitution Scheme Accounting records were manipulated to misappropriate funds by using a check for cash substitution scheme. Payments from a variety of sources, some of which are identified below, were received at the recreation center. However, accountability for these revenue transactions was never established on the computer cash register system. When checks from these sources were deposited in the bank as a part of the recreation center's deposit of cash receipts, a corresponding amount of cash was stolen. Checks received through the mail or over-the-counter from the following sources were not properly accounted for and controlled as revenue transactions at the recreation center.

(a) Checks From Vendors On two 1994 business days reviewed during this audit, checks from a vending machine company and a recycling company were included in the recreation center's bank deposits. However, accountability was not recorded on the computer cash register system for these revenue transactions. These check payments represented valid revenue transactions for amounts owed the recreation center for routine business activities. The amount of loss from this method was \$85.90.

(b) Checks From Customers On eight business days reviewed during this audit, checks from customers for a wide variety of services were included in the recreation center's bank deposits. However, accountability was not recorded on the computer cash register system for

these transactions. Since these check payments represented valid transactions, these customers actually received the service as indicated by the recreation center's pass and class records. The amount of loss from this method was \$620.00.

(2) Missing Funds After Computer Cash Register Merge Failures On certain occasions, operational problems occurred in the computer cash register system when fund accountability records from cash register No. 2 were merged with fund accountability records from cash register No. 1 during end-of-day processing. As a result, the accounting records from cash register No. 2 were lost. Sometimes these record losses were manually added to the accounting reports to establish accountability for the funds associated with these transactions. However, in other cases, accountability for the funds associated with these transactions was not noted by the office specialist or recorded in the accounting records when these operational problems occurred. As a result, no one independent of the cashier function was aware that financial losses had occurred. The amount of loss from this method could not be determined.

When we discussed these cash receipting irregularities with employees at the recreation center, they were unable to provide any reasonable explanation for the missing funds.

As a result of the lack of adequate internal controls at the recreation center as described below, it was not possible for either managers or auditors to fix responsibility for these losses to any single individual.

RCW 42.20.070 states:

Every public officer, and every other person receiving money on behalf or for or on account of the people of the state or of any department of the state government or of any bureau or fund created by law in which the people are directly or indirectly interested, or for or on account of any county, city, town, or any school, diking, drainage, or irrigation district, who:

(1) Shall appropriate to his or her own use or the use of any person not entitled thereto, without authority of law, any money so received by him or her as such officer or otherwise; or

(2) Shall knowingly keep any false account, or make any false entry or erasure in any account, of or relating to any money so received by him or her; or

(3) Shall fraudulently alter, falsify, conceal, destroy or obliterate any such account; or

(4) Shall willfully omit or refuse to pay over to the state, its officer or agent authorized by law to receive the same, or to such county, city, town, or such school, diking, drainage, or irrigation district or to the proper officer or authority empowered to demand and receive the same, any money received by him or her as such officer when it is a duty imposed upon him or her by law to pay over and account for the same, shall be punished by imprisonment in a state correctional facility for not more than 15 years.

The following internal control weaknesses allowed this misappropriation of public funds

at the recreation center to occur and not be detected in a timely manner.

- a. There was an inadequate segregation of duties. Most of the accounting functions were the sole responsibility of one person, the office specialist. However, there was no periodic review or monitoring of the office specialist's work by other facility management officials who were independent of the accounting function to ensure that all functions were properly accomplished.
- b. While mode of payment information (i.e., transactions by check or by cash) was recorded in the computer cash register system, the office specialist did not use this information to reconcile daily accounting records with the bank deposit. In addition, management officials did not periodically review the check and cash composition of bank deposits to ensure this information agreed with the actual accounting records produced by the computer cash register system.
- c. All appropriate accounting reports from the computer cash register system, while available, were not produced or used to assist in the financial management of the facility.

(1) Since only records from November 1993 are currently maintained on the computer cash register system, and since the daily accounting reports were not produced over time, there is no permanent record of all cash receipt transactions at the recreation center. Thus, the accounting records for most of calendar year 1993 are unauditable.

(2) At least three accounting reports are critical to the successful operation of the facility. These are: (a) the General Ledger Posting Log Report; (b) the Journal Summary Report; and, (c) the Journal Detail Report. Prior to May 1, 1994, only the General Ledger Posting Log Report was produced and submitted to the finance department with a copy of the daily bank deposit slip. After May 1, 1994, when irregularities in accounting procedures were detected by the finance department, the Journal Summary Report was produced to assist in balancing daily accounting records by mode of payment. However, the Journal Detail Report was not produced until approximately mid-June 1994 after additional cash receipting irregularities were presented to employees and managers. This latter report is one of the most important documents available to management officials because it provides a detailed listing of all cash receipt transactions each business day. While this report can be used for a variety of management purposes, it is essential to properly reconcile differences between the accounting records and the bank deposit.

(3) Managers did not use available management reports to monitor the annual budget. As a result, there was no mechanism in place to control all revenue sources which were available to the recreation center, or to monitor any revenue shortfalls which indicated problems needing attention by management officials. When we compared revenue for the first five months of 1993 to revenue during the same period in 1994, we found a decline in revenue of approximately \$13,000. On an annual basis, this loss of revenue would be approximately \$31,000.

- d. There were no procedures to ensure that accountability for all revenue received through the mail was properly accounted for and controlled. No one independent of the cashier function opened the mail and made a list of these revenue transactions for control purposes. As a result, practically everyone in the facility picked up the mail, opened the envelopes and removed the checks, and recorded

cash receipt transactions in the computer cash register system.

- e. Bank deposits were not made intact daily. Bank deposits were only made Monday through Friday to match the work schedule of the office specialist. In addition, cashiers cashed personal checks for city employees from daily cash receipts. However, this practice ceased in late April 1994, when irregularities in accounting procedures were detected by the finance department.
- f. Access to the two safes was not appropriately restricted. Practically all employees know the safe combinations, and the combinations were not changed periodically or when employees terminated employment.
- g. Practically all employees have the ability to process "void" transactions on the computer cash register system. While copies of these "void" transactions were produced by the computer cash register system at the time the transactions were recorded, these documents were not approved by a supervisor or retained on file as a part of the daily accounting records. In addition, no one in the facility monitored this high risk transaction type to ensure that all transactions were valid.
- h. Cash receipt transactions were not always accurately recorded on the computer cash register by cashiers or properly monitored by supervisors. Customer names were not always entered at the time cash receipt transactions were recorded, the mode of payment was not always recorded accurately, and customer checks were not always imprinted by the computer cash register endorsing function to properly record all transaction information on the reverse side of each check accepted at the facility. These conditions make it difficult to reconcile daily accounting records with the bank deposit.
- i. While the computer cash register system has the capability for individual passwords to be assigned to all cashiers, this function was not used. Thus, it was not possible for either managers or auditors to determine who processed individual cash receipt transactions.
- j. It was not possible for either managers or auditors to fix responsibility for cash receipts to individual cashiers. Cashiers did not count or accept responsibility for the change fund at the beginning of each work shift, and cashiers did not document the transfer of accountability for cash receipts and the change fund from one work shift to another or from the evening shift to the office specialist at the end of the business day.
- k. The office specialist did not properly use the computer cash register accounting reports to monitor the cashier function and ensure that all transaction numbers used were properly accounted for each business day. Under existing procedures at the facility, cash register No. 2 is merged with cash register No. 1 at the end of the evening work shift. This task was not restricted to a supervisor and could be performed by any cashier on duty in the facility. Occasionally, operational problems occurred during this merging process. As a result, the accounting records from cash register No. 2 were lost. Sometimes these record losses were manually added to the accounting reports to establish accountability for the funds associated with these transactions. However, in other cases, accountability for the funds associated with these transactions was not noted by the office specialist or recorded manually in the accounting records when these operational problems occurred. As a result, no one independent of the cashier function was aware that financial losses had occurred.

- l. Employees did not appear to have been adequately trained in the operation and management of the computer cash register system used in the facility.
- m. While cash overages and shortages from cashier operations at the recreation center were recorded in the city's accounting system, the office specialist maintained a personal "slush" fund in her office desk drawer to cover minor cash overages and shortages in the change fund.
- o. Accountable forms for a wide variety of passes and classes were not prenumbered or controlled at the recreation center. As a result, it was not possible for either managers or auditors to determine whether the revenue associated with all forms used at the facility was properly accounted for and controlled.

We recommend the city seek recovery of the misappropriated \$2,167.75 and related audit/investigation costs from their insurance bonding company.

Bond coverage for city employees is as follows:

Hartford Fire Insurance Company
Public Employee Dishonesty
Policy No. PEB J12863
\$250,000
March 1, 1993, until cancelled

We also recommend the Washington State Office of the Attorney General and the Pierce County Prosecuting Attorney review this matter and take whatever action is deemed necessary under the circumstances. Any compromise or settlement of this claim must be approved in writing by the Attorney General and State Auditor as directed by RCW 43.09.260.

We further recommend the city:

- a. Review its overall accounting controls at the recreation center, correct the weaknesses identified above, and implement an effective system of internal control designed to ensure the protection of public assets.
- b. Notify the insurance bonding company of this loss of funds.
- c. Retain all accounting records in accordance with the required retention policy.